ACTIONABLE AFRICAN BUSINESS RISK INTELLIGENCE

ALGERIA:

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FOREX PRESSURES WILL DETERMINE ANY POST-ELECTION POLITICAL TRANSITION

Ahead of next year's elections, the government will maintain the political status quo and boost welfare spending in order to curb any outbreaks of unrest; yet falling foreign exchange reserves will determine longer term succession scenarios and pose a nascent threat to repayment schedules as debt balloons.

On 28 October, the head of the governing Front de Libération Nationale (FNL) party, Djamel Ould Abbes, announced that President Abdelaziz Bouteflika will seek a fifth consecutive term in elections slated for April 2019. The 81-year old and frail Bouteflika, whose last public address dates to more than six years ago, has yet to officially announce his candidacy. Several months ago, there were mounting rumours that the head of state may already have passed away or has been further incapacitated since a previous stroke. All major players in Algeria have since called on Bouteflika to stand for a fifth presidential term next year, indicating that they have still not found a suitable successor to replace him.

Succession candidates

Presidential brother Saïd Bouteflika has been most vocal in his support for his brother's fifth term, which has triggered rumours that he still seeks to succeed his brother, despite his lack of popularity by the military and the public. Other contenders for the succession, such as Vice-Minister of Defence and Army Chief of Staff Lieutenant General Ahmed Gaïd Salah, have also fallen into line to support the continuity of power for the next year. Prime Minister Ahmed Ouyahia, who harbours similar succession ambitions, has also supported a fifth term in office for Bouteflika, alongside other senior politicians, union leaders, and generals.

Algeria's balance of power has been further upset recently by a purge of party officials and a series of politically motivated corruption investigations ahead of next year's elections. According to local source reports, the judicial and security sector reshuffle was instigated by Saïd Bouteflika and his political and business allies, such as the Forum des chefs d'entreprise (FCE) head Ali Haddad. It seems that key Bouteflika allies are fearing political upheaval next year around the elections and the threat of prosecution against themselves, should President Bouteflika be incapacitated or die in office. A Haddad ally, advertising mogul Mourad Hadj-Saïd is already under investigation for abusive business practices.

The balance of power

Since the 2017 parliamentary elections, Army Chief of Staff Ahmed Gaïd Salah has formed a tentative alliance with Prime Minister Ahmed Ouyahia to hold together Algeria's political and security establishment, in conjunction with the Bouteflika faction. Prime Minister Ouyahia's smaller Rassemblement Nationale Démocratique (RND) party has taken up the mantle as the pro-business party in the Algerian parliament. Prominent business leaders and elected RND lawmakers have been pleading for the lifting of export restrictions.

While Gaïd Salah is charged with upholding the security of the state, Ouyahia is seeking to repair the distressed oil-dependent economy. Their loyalty to President Bouteflika has allowed the latter's faction to maintain its dominance, giving huge influence to the president's brother Saïd Bouteflika and business associates such as Ali Haddad. These figures have over the past few years taken a cautious embrace of public-private partnerships and lobbied for the partial liberalisation of the country's economy.

It is therefore unsurprising that the principal influence brokers in Algeria's power balance have been reluctant to disrupt the status quo by seeking a replacement as head of state. The main arbiter of power between the various factions remains Minister of State and Presidential Counsellor Boualem Bessaieh. Bessaieh, who is likely to play a crucial role in the eventual transition, will have to manage the negotiations for a transfer of power between influential factions. This power play seems to be on hold until at least after the 2019 elections.

Economic boon

As a result of the apparent political stability, Algeria's economy has benefited from a relative period of political stability. The economy has recently benefited from increased gas output, a relative recovery in the Eurozone, and higher oil prices. State oil company Sonatrach's chief executive Abdelmoumen Ould has also encouraged improved relations with international oil companies, which has advanced foreign investment. Last month, Italian oil major Eni struck a deal to team up with French major Total to explore oil and gas in Algeria.

Algeria is seeking to increase oil output to boost revenues following a crash in prices in 2014. The recent rebound in prices has allowed Sonatrach to invest in petrochemicals, unconventional, and offshore exploration. Eni has also agreed with Sonatrach to take a 49 percent stake in three oil blocks in the North Berkine basin which are estimated to hold 145 million barrels of oil. France's Total has also signed a USD1.5 billion petrochemical deal with Sonatrach, recently stating that its confidence in Algeria's oil industry had been restored.

Algeria's economy has therefore been making a steady recovery from its near-collapse in 2014. Annual inflation fell to 4.7 percent in September from 4.8 percent the previous month after a slight decline in price of some foodstuffs. The country has been trying to boost domestic output and cut imports in an attempt to cope with financial pressures caused by a fall in energy earnings since 2014.

Energy earnings rose 14.86 percent in the first nine months of 2018 from the same period a year ago, reducing the country's trade deficit by 56.71 percent. Oil and gas exports, which accounted for 93.08 percent of total sales abroad, reached USD27.93 billion, up from USD24.32 billion in January-September 2017. The overall value of exports reached USD30.012 billion against USD25.697 billion in the first nine months of 2017, while imports fell 1.52 percent to USD33.703 billion. The government has imposed import restrictions for some products in a bid to cut spending on purchases from abroad. In addition to import controls, the '51/49 rule', which limits foreign participation in any energy project's equity, is expected to remain in place.

Socio-economic frustrations

The threat of political uncertainty over the succession and the upheaval caused by the reshuffles and corruption probes are likely to be intensified by socio-economic grievances which are again rearing their head. Frustrated young urban populations are becoming increasingly critical of the political power play, corruption, and cronyism in Algeria's elite. Meanwhile, the economic recovery has failed to take hold among Algeria's urban youths, threatening liberalizing reforms pushed through by Ouyahia's government over the past year.

Algerians complain of the erosion of their purchasing power as prices have risen and their currency has depreciated, recalling the strikes staged this year by thousands of doctors and teachers for better pay and working conditions. As to Algeria's economic liberalization, it remains selective, tightly managed and potentially reversible if oil prices rise or if Bouteflika is no longer president. It is likely that the country's efforts and commitment to diversify its economy will weaken if oil prices continued to rise in the global market.

The government will seek to avoid any policies that would risk triggering fresh anti-austerity protests.

Therefore, Prime Minister Ouyahia is unlikely to implement the spending cuts required by the International Monetary Fund (IMF). Instead, he will continue to fund the ballooning budget deficit with quantitative easing by the central bank. Nevertheless, spontaneous riots and protests over issues like unemployment or proposed subsidy reform remain a present risk. The government remains deeply wary of social unrest threatening the stability of the state and of Islamist influence, and is proactive in using public expenditure and highly capable security forces to discourage protests.

If protests did escalate and become co-ordinated in major cities – involving tens of thousands of people or shutdown of key infrastructure such as ports – the army would have to decide whether to use force to suppress them, potentially inflaming the situation and leading to a popular rejection of the army, or to oust the civilian leadership and call fresh elections. We consider such a scenario unlikely for 2018/19.

Risk implications:

It is unlikely that civil unrest will pose a serious threat to political stability ahead of the elections. Instead, such unrest may become more prevalent following any eventual transition from President Bouteflika. For Prime Minister Ouyahia, implementing a successful and broad-based economic recovery will be crucial for his succession ambitions. A succession by Ouyahia under a revived economy would be the lowest risk scenario following next year's elections. However, there remain serious challenges ahead.

The government has reversed plans to cut the budget and will continue high-level spending in the upcoming election year. In September, The government released a draft budget of USD71.9 billion for 2019, which would finance free housing programmes, agricultural and water development, infrastructure and subsidies on consumer goods. It would result in a deficit equal to 9.2% of GDP.

The rise of oil prices has been a boon to Algeria's economy, emboldening the government to keep up its high spending. Algeria's government adopted what is known as an "easy money" approach, using the Central Bank to buy assets, including government debt with long-term maturity, to finance the deficit and high spending of 2018.

However, continued high spending into next year is likely to fuel an increase in imports, causing the country's foreign currency reserves to shrink and prompting it to borrow from abroad, a trend the government has struggled to avoid so far. The Finance Ministry said it expects current account deficits of USD17.9 billion in 2019, USD14.5 billion for the year after and USD14 billion in 2021. However those estimates seem unrealistic as foreign exchange reserves shrink due to the continued high social welfare spending.

Based on independent estimates, foreign currency reserves will fall to USD62.5 billion in 2019, then USD47.8 billion for 2020, and USD33.8 billion for the following year. The government has previously vowed to keep foreign currency reserves lower than USD100 billion, which now seems effectively impossible. As a result, the Algerian government is expected to seek additional foreign debt to finance next year's election budget, as well as future sending commitments.

The Central Bank of Algeria allocated loans of more than USD 80 billion to public and private sectors in the first half of 2018, a 6 percent increase compared with a year ago. More than 54 percent of the loans are long-term credits allocated to state-run companies in the hydrocarbons sector. Loans allocated to the private sector amounted to some USD40 billion, with an increase of 4.3 percent over the same period last year.

As a result, Prime Minister Ouyahia' s planned economic recovery may be undermined in the longer term by inflation and the depreciating value of the Algerian dinar, which would ultimately wreck his chances to succeed Bouteflika. In such a scenario, a succession by Saïd Bouteflika or General Ahmed Gaïd Salah would become more likely, thus posing higher risk of unrest and economic disruption.